



ROYAL LONDON GLOBAL SUSTAINABLE EQUITY FUND

Quarterly Report 30 June 2021

For professional clients only, not suitable for retail investors

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Top ten holdings

	Fund (%)
Microsoft	4.6
Taiwan Semiconductor Manufacturing Company	3.8
Thermo Fisher Scientific	3.5
Adobe	3.4
Amazon	3.3
Adidas	3.2
Texas	3.2
ASML Holding	3.1
Alphabet	3.0
AstraZeneca Plc	2.8
Total	34.0

Source: RLAM, based on the M Acc share class.

Fund data

	Fund
No. of stocks	43
Fund size	£142.1m
Launch date	25.02.2020

Performance

	Fund (M Acc) (%)	Benchmark ¹ (%)	Relative (%)
Q2 2021	11.55	7.26	4.29
Year-to-date	9.92	11.12	-1.20
Rolling 12 months	26.75	24.56	2.19
Since inception 25.02.2020	29.50	20.06	9.44

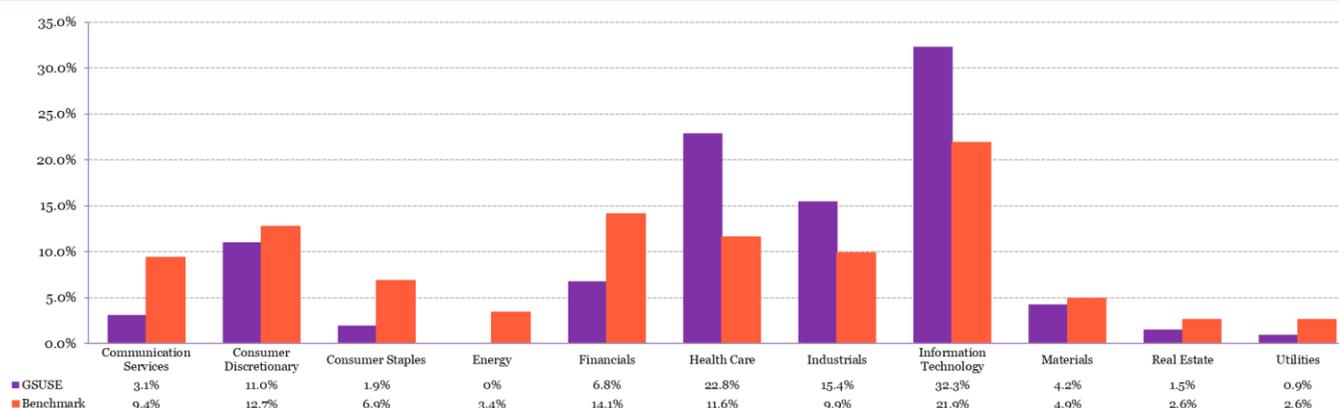
Past performance is not necessarily a reliable indicator of future performance. The value of investments and the income from them is not guaranteed and may go down as well as up and investors may not get back the amount originally invested.

All performance figures stated gross of fees and tax unless otherwise stated.

Source: RLAM, gross of fees.

¹Benchmark: MSCI All Countries World Net Total Return Index GBP.

Sector breakdown



Source: RLAM. Figures in relation to your portfolio exclude the impact of cash held.

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Executive summary

- India was a particular concern during the second quarter, with daily new case numbers hitting new records for any country. The 7-day average of new cases fell in the US and Euro area during April, though continued to rise in Germany; social distancing decisions were mixed. A state of emergency was announced in parts of Japan (incl. Tokyo and Osaka). Meanwhile, the EU's vaccination programme made headway and Commission President von der Leyen said that the EU will have enough doses to vaccinate 70% of adults in July.
- The fund outperformed this quarter, helped by equity markets moving away from the 're-opening trade' that has dominated markets since November, and starting to look more at individual companies and their fundamentals.

Market overview

- The MSCI World Index posted healthy returns of 7.88% through the second quarter of 2021. Performance was strong throughout, although May was slightly less positive than the preceding and following months and was markedly more volatile. Regionally, Japan was again the only market to post negative returns in sterling terms (-0.33%) while the US (8.9%) continued to lead major equity market returns, followed by Europe ex. UK (8.16%), the UK (5.81%), and emerging markets (5.08%).
- Growth returned as the main driver of performance in the quarter; the MSCI World Growth Index returned 10.94% for the quarter versus 4.9% for the MSCI World Value Index. The outperformance of growth was driven by the information technology sector, which grew by 10.6%, leading global sector returns. Energy (9.6%) and healthcare (9.5%) were the next best performing sectors, while financials, the second strongest sector in the first quarter, was the sixth best of 11 MSCI sectors in the second quarter, providing returns of 6.42% to investors.
- In UK bond markets, after a first quarter focused on rising inflation expectations and a corresponding increase in government bond yields, the benchmark 10-year gilt yield fell from 0.85% to 0.72% over the quarter: the gilt market returned 1.70% on an all maturities basis (FTSE Actuaries). In sterling investment grade credit, the market returned 1.71%. The average sterling investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) tightened from 0.96% to 0.91%.
- The Brazilian real was the strongest currency in the quarter gaining 11.8% against the (US) dollar, however major currencies were largely sedentary in comparison. The euro strengthened by 0.83% versus the dollar, while sterling saw no significant movement. The Australian dollar was the period's weakest currency, losing 1.61% against the US dollar for the quarter.
- Commodities extended their rally, leading cross-asset returns. Oil prices continued to recover strongly and were up 50% year-to-date, reaching their highest levels since October 2018 as the reopening trade sustained and blockages in supply chains continued to impact prices. The price of Brent crude oil rose by 18.2% to more than \$76 a barrel, while copper and gold also gained value; copper was up 7.2% for the quarter, and gold prices grew by 3.5% to \$1,791/oz.

Performance and activity

- Our sustainable strategies are orientated to those companies that have a positive impact on society and create value for investors through access to long-term growth markets and innovation. Areas such as healthcare and technology remain at the core of the equity portfolios, complemented by engineering, utilities, selected financial services, and companies that lead their industries in ESG performance.
- While the Sustainable funds have different mandates, risk profiles, asset mixes and geographical exposures, equity exposure is driven by the same underlying team, philosophy and process. Many of our key stocks will be held across multiple portfolios.
- The fund outperformed its benchmark over the quarter returning 11.4% against benchmark return of 7.3% on a net of fees basis for the M Acc share class. The fund benefitted from its exposure to Adidas and Novo Nordisk, as well as its tech exposure in Adobe and Intuit, although exposure to Phillips did detract from returns.
- **Adidas** was a major contributor to performance. The shares had lagged in the first quarter on the Chinese government insisting the removal of Adidas from various e-commerce platforms following its statements around not using cotton from the Xinjiang region due to accusations of forced labour. However, this does not seem to have had a material impact on overall Group sales, with products being relisted, while the company announced a strong set of results, all of which helped reverse the earlier underperformance. **NovoNordisk** was another positive for the fund. Diabetes and weight management remain societal issues and we see the company – the world's largest producer of insulin – as part of dealing with this better over the long term. The shares performed well in the quarter as it had its weight management drug approved by the US Food and Drug Administration (FDA) – the first such treatment the FDA has approved since 2014. Finally, one trend we have seen with the end of the 'reopening trade' was a rebound from technology stocks, with our holdings in **Adobe** and

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Intuit adding to performance, helped by strong results at both. Against this, our exposure to **Phillips** was negative. The firm recalled a ventilator component and although there are no reports of this causing any issues prior to recall, the market took a ‘shoot first’ approach given the potential for litigation.

- We feel optimistic for the remainder of the year. While markets can be unpredictable, we believe that markets are more balanced now in the aftermath of the rotation. We think the window of opportunity for buying Covid recovery stocks has closed, and we are not yet convinced about the arguments for inflation returning in the long term. As a result, buying more of what we own at lower prices makes more sense to us than chasing market trends.
- Notable trades this quarter included adding to our position in **Trane Technologies** in the US, a global leader in heating, ventilation and air-conditioning (HVAC) systems and in refrigerated transport. Its solutions bring efficient and sustainable climate innovations to buildings, homes and transport. We see an attractive growth outlook for the company and room for margins to expand over the coming years. We also initiated a new position in **Schneider Electric**. The French company is highly aligned with themes such as electrification and industrial efficiency. As a leading component manufacturer, Schneider will be a key part of the supply chain for those looking to expand renewable energy capabilities. We often look for this sort of investment – where perhaps the ‘obvious’ choice of companies may be expensive, but looking at those that offer complementary products and services are relatively cheap. In addition we added **Sika** to the portfolio. The Swiss chemicals company produces chemicals that help make the construction industry more efficient. Construction is typically a poor sector in terms of carbon footprint, and 70% of Sika’s products are focused on improving this. The company is also well placed to be a prime beneficiary of infrastructure spend such as the US \$2trn investment programme announced in April.

Outlook

- There may be short-term challenges if new strains of Coronavirus spread quickly, however central banks remain firmly committed to supportive monetary and fiscal policies.
- Despite a likely short-term spike in inflation, we are not yet convinced about the arguments for inflation returning in the long term. Our view is that it is more likely that the pandemic will be a long-lasting *deflationary* force as technology reduces our dependence on finite physical resources. 2021 could be like 2009, which was a cyclical/value market as economies normalised after the financial crisis: 2009 was also a year of inflation concerns, as quantitative easing and an economic recovery kicked in. This of course proved to be incorrect and 10 years of subdued inflation followed. There are of course critical differences between 2021 and 2009: in 2009 stimulus was used to prop up the banking sector, whereas today it is being used to feed consumption. Equally, back in 2009 central banks wanted to keep inflation down, now they want to see higher inflation. Still, the point stands.
- Easing inflation will generally benefit strategies such as ours. By its very nature, sustainable investing is a long duration strategy – as it picks out companies and trends that will take many years to fully develop. This can be seen in our turnover figures, which in the last 12 months is about 10% for the equities we own, suggesting an average holding period of 10 years. And what we have seen historically in our performance is that while market trends ebb and flow in our favour, fundamentals do dominate over the long term, and these will remain the key drivers of our portfolios.
- A lot of client conversation in recent months have been about growth or value investing styles, their merits and the impact on sustainable investing. Equity markets saw a rotation out of growth and into value stocks from November 2020 into 2021. There are now signs that this trend has reversed once more. RLAM’s Sustainable funds take a long-term view: we are looking at companies that may benefit from trends that play out over multiple years and even decades. This is what drives our investment choices and ultimately performance, rather than a preference for growth over value.
- With these various factors, we believe that equities will outperform bonds over the year. We feel that forecasts of strong GDP growth in the coming months aren’t fully reflected in earnings forecasts yet, particularly for more cyclical companies, so sectoral rotation may persist in the short term. Beyond that, there are signs that we may be in the later stages of a long-term bull market that started after the global financial crisis in 2009. These include the recent Deliveroo IPO, the rise of SPACs (special purpose acquisition companies – the ‘new’ driver of global M&A) and the Gamestock phenomenon. However, these later stages can go on for a while, particularly with such widespread central bank support. We have therefore maintained our pro equity stance in the mixed asset strategies as we remain positive on the medium- to long-term outlook of the specific companies we invest in.

A long history of sustainable investing

- You can find more information on our sustainable funds and our views on sustainable investing and other ESG-related issues at www.rlam.co.uk.

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